IN THE UNITED STATES DISTRICT COURT FOR THE

EASTERN DISTRICT OF TENNESSEE

WINCHESTER DIVISION

FARMERS BANK AND TRUST COMPANY,	)	
Plaintiff,	)	
v.	)	No. CIV-4-79-15
TRANSAMERICA INSURANCE COMPANY,	)	
Defendant.	)	

MEMORANDUM OPINION

(Filed November 20, 1980)

The defendant Transamerica Insurance Company agreed in a banker's blanket bond to indemnify and hold harmless the Farmers National Bank (now the plaintiff Farmers Bank & Trust Company) for *inter alia* loss through such bank's having, in good faith and in the course of business, extended credit on the faith of documents or other written instruments which proved to be forged as to the signature of any person signing it in any capacity. Such bank sustained a loss through having, in good faith and in the course of business, extended credit on the faith of a certain document or other written instrument. The signature thereto of Mr. D. M. Hill was essential to its validity. It is undisputed and agreed that Mr. Hill, who was deceased pretrial, did not sign such document or instrument. Mr. R. L. Herring, who stood to profit from the fraud and deceit of a forgery thereto of Mr.

Hill's name, declined under privilege against incriminating himself, Constituton, Fifth Amendment, to testify whether he (Mr. Herring) had thus forged Mr. Hill's name.

Only if Mr. Hill signed his own name to the instrument in question or caused it to be signed for him or ratified it would it not have been a forgery. *United Pacific Insurance Co. v. Idaho First National Bank*, C. A. 9th (1967), 378 F. (2d) 62, 68-69 [12]. ("• • • If one James C. Bolton signed his own name, the signature would not be a forgery • • •"). "• • • [A] signature may be made for a person by the hand of another who acts in the presence of such person at his direction, request or with his acquiescence. • • • [A] person may adopt a signature written for him by another by a subsequent approval or ratification. • • •" *Stoots v. State* (1959), 205 Tenn. 59, 73 (9, 10), 325 S. W. (2d) 533.

While the agreement of the parties defines some of its terms, the term "forgery" evidently is not defined therein; therefore a "forgery" in Tennessee within the contemplation of this agreement "• • • is roughly equivalent to an act which, under applicable principles of criminal law, would amount to the crime of forgery." Anno: Insurance-Forgery-What Constitutes, 52 A. L. R. (2d) 208, § 2. The only time the Supreme Court of Tennessee appears to have discussed the act which, under principles of criminal law, amounts to the crime of forgery it said *inter alia*:

• • • • •

> • • • Forgery at common law denotes a false making. • • • a making, *malo animo*, of any written instrument for the purpose of fraud and deceit. • • • The crime of forgery is defined by Section 10979 of the Code as follows: "Forgery is the fraudulent making or alteration of any writing to the prejudice of another's rights." [*Accord*: T. C. A. § 39-1701.]

> * * * There can be no doubt that there must be fraudulent intent to constitute the offense. Moreover, the writing must be of some legal efficacy, real or apparent, since otherwise it has no legal tendency to defraud. * * *

Mallory v. State (1943), 179 Tenn. 617, 619 (1)-620 (2), 168 S. W. (2d) 787. *First Nat. Bank of Memphis v. Aetna Casualty & Surety Co.*, C. A. 6th (1962), 309 F. (2d) 702, 705 [4], certiorari denied (1963), 372 U. S. 953, 83 S. Ct. 951, 9 L. Ed. (2d) 977, dealt with certain instruments which had been signed and issued regularly by persons authorized so to do; as the terms forgery and counterfeited were understood in common parlance, the genuineness of the execution of these instruments would not be considered as forged or counterfeited "* * * and certainly not at common law or under the statutes of Alabama or Tennessee. * * *" *Ibid.*, 309 F. (2d) at 705 [4].

It was incumbent upon the defendant to establish satisfactorily its defense that Mr. Hill's signature was affixed to the instrument by the hand of another in a legally binding manner. *Aetna Life Ins. Co. v. Ward* (1891), 140 U. S. 76, 11 S. Ct. 720, 35 L. Ed. 371, 375 (headnote 6). This it did not do. However, this was a defense with sufficient merit to justify the defendant's refusal in good faith to pay the claim of the plaintiff on demand until after this adjudication.

For the purposes of ths lawsuit only, the Court infers and hereby FINDS that Mr. Hill's name was signed to the instrument in question by Mr. Herring under circumstances which constituted a false making thereof, for the purpose of deceit and with a fraudulent intent; that such instrument had a definite legal efficacy; and that such forgery, relied on by the bank's personnel in extending credit,

was such a proximate factor in causing the bank's loss that the situation constituted one of coverage under the agreement of the parties. (Especially as to the final finding,) *cf. First Fed. S. & L. Ass'n of Beresford, S. D. v. Aetna Ins. Co.*,* C. A. 8th (1970), 431 F. (2d) 267, 269-270 [1].

The loss of the bank because of such forgery was in the principal amount of $176,743.56; the defendant did not agree with the plaintiff to indemify and hold harmless the Traders National Bank for any loss it might sustain because of a covered forgery. The bank is entitled to recover also prejudgment interest thereon; the fair, average rate of interest in the pertinent period was 10%, and such interest amounts to an aggregate of $36,995.09.

Based upon the foregoing findings of fact and conclusions of law, it is the decision of this Court that the plaintiff Farmers Bank & Trust Company recover of the defendant Transamerica Insurance Company the sum of $213,738.65. No penalty is imposed additionally. Rule 58 (1), Federal Rules of Civil Procedure.

FILE:

/s/ C. G. NEESE

United States District Judge

Marland Casualty Co. v. American Trust Co., C. C. A. 5th (1934), 71 F. (2d) 137, cited to the Court, is inapposite because it pertains to a situation where the fiduciary obligations of the president of the bonded bank to the bank had been breached., *ibid.*, at pp. 138-139 [2].

No. 80-5486

UNITED STATES COURT OF APPEALS

FOR THE SIXTH CIRCUIT

FARMERS BANK & TRUST COMPANY OF WINCHESTER, TENNESSEE, *Plaintiff-Appellee,* v. TRANSAMERICA INSURANCE COMPANY, *Defendant-Appellant.*	ON APPEAL from the United States District Court for the Eastern District of Tennessee.

Decided and Filed March 29, 1982.

Before: MERRITT and JONES, Circuit Judges; TAYLOR, District Judge.*

MERRITT, Circuit Judge. In this diversity case from Tennessee, the defendant, Transamerica Insurance Company, appeals from a judgment of the District Court granting the plaintiff, Farmers Bank and Trust Company (Bank), recovery under a bankers blanket bond in the amount of $213,738. The bank's claim for recovery under the blanket bond arises out of a fraudulent sale-leaseback transaction for heavy earth-moving equipment which the bank financed. We do not agree with the District Court's conclusion that the bank's loss was covered by the blanket bond. The District Court allocated the burden of proof on the question of forgery incorrectly and this error led it to make erroneous findings of fact on the issue.

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* The Honorable Anna Diggs Taylor, Judge, United States District Court for the Eastern District of Michigan, sitting by designation.

Standard Leasing Corporation purchased in November 1977, a Caterpiller loader and two Caterpillar bulldozers from Herco Corporation, owned by Robert L. Herring. Standard leased them back to Herco under a contract calling for Herco to pay sixty monthly installments of $8,000 per piece of equipment. Standard then assigned the contract to the bank for a consideration of approximately $363,317. Accordingly, the bank became Herco's creditor and lessor. During negotiations, Standard gave the bank several supporting documents – among them, a bill of sale for the three pieces of equipment. The bill of sale bore the signature of David M. Hill and recited that City Fuel Oil Company, owned by Hill, had sold the equipment to Herco on September 12, 1977.

Robert L. Herring, owner of Herco, after making payments of $8,914.97, defaulted on the lease. The bank discovered that the equipment did not exist and had never been in the hands of Hill, Herring or Herco. The bank later discovered that the signature of David M. Hill had not been penned by Hill but rather had been affixed to the bill of sale by Robert L. Herring.

The bank filed a claim against Transamerica for the loss under Clause (E) of its blanket bond. Clause (E), a standard provision in bankers blanket bonds, covers:

> *(E) Loss* (1) through the insured's having . . . purchased . . . on the faith of, or otherwise acted upon . . . written instruments which prove to have been
>
> (a) counterfeited or *forged as to the signature of any maker* (emphasis added).

The bank maintained that the signature of Hill on the bill of sale was forged. Transamerica refused to indemnify the loss relying upon the exclusions provided in Section (2) of the bond. The applicable portion of the exclusion section provides:

Section 2 THIS BOND DOES NOT COVER:

(e) loss resulting from . . . default upon,

. . . any transaction in the nature of . . . a loan made by . . . the insured or . . .

agreement or other evidence of debt assigned or sold to . . . the insured, whether procured in good faith or through trick, artifice, *fraud* or false pretense, unless such loss is covered under [Clause E]. (emphasis added)

Transamerica does not dispute that there was a fraud on the bank but maintains that unless the fraud is accompanied by a forgery "as to the signature of any maker," as required by Clause (E), the loss is not covered.

Transamerica argues that the District Court's finding that the bill of sale was a forgery was clearly erroneous. As the District Court stated in its opinion, a person is not guilty of forgery if he signs another's name with authority to do so, or if the signature is subsequently ratified. The question is whether David Hill authorized Robert Herring to sign Hill's name on the bill of sale or whether Hill ratified the signature. Transamerica makes two points: (1) that the burden of proof for the authority-ratification issue lay with the bank as an element of its case to establish a forgery and that the court improperly placed the burden of proof on Transamerica; and (2) that the bank failed to prove lack of authority or ratification and that Transamerica's evidence in rebuttal clearly established authority.

It is elementary in insurance law that a claimant under an insurance policy has the initial burden of proving that he comes within the terms of the policy. J. Appleman, 21 Insurance Law and Practice § 12091 (1980). 46 C.J.S. *Insurance* § 1316 (1946). Conversely, the insurer carries the burden if it claims that one of the policy exclusions applies to the claimant and prevents recovery. In the court below the

judge concluded that "[i]t was incumbent upon the defendant to establish satisfactorily its defense that Mr. Hill's signature was affixed by the hand of another in a legally binding manner . . . . This it did not do." Thus the District Court put the burden of proving the forgery on the defendant insurance company.

It is necessary to consider the way the bankers blanket bond is drafted in order to determine which party had the burden of proof on the signature question. Bankers blanket bonds are generally drafted with standard clauses which describe both the coverage and the exclusions. In the standard Clause (E) provision, the bank is protected against losses resulting from the purchase of documents or other written instruments which prove to have been forged. Forgery coverage is optional. In some blanket bonds, such as the one here, express protection against forgeries is provided. In other policies, the insured may elect not to buy forgery protection and the policy may include an express exclusion for loss caused by forgery. *E.g., American National Bank and Trust Co. of Bowling Green, Kentucky* v. *Hartford Accident and Indemnity Co.*, 442 F.2d 995 (6th Cir. 1971).

The general rule applies to determine the allocation of the burden of proof whether losses from forgeries are covered risks or excluded losses. The one suing on the bond has the burden "to prove all of the facts essential to a recovery," J. Appleman, 21 Insurance Law and Practice § 12294 at 350 (1980), and the insurer has the burden of proving exclusions. *E.g., Calcasieu-Marine National Bank of Lake Charles* v. *American Employers' Insurance Co.*, 533 F.2d 290, 295 (5th Cir. 1976), *cert. denied sub nom, Louisiana Bank & Trust Co.* v. *Employers Liability Assurance Corp.*, 429 U.S. 922 (1976) (burden on insurer to show exclusion of coverage under bankers blanket bond). Therefore, the bank must prove forgery in order to recover under a bankers blanket bond. *Fidelity and Casualty Co.* v. *Bank of Commerce*, 285 Ala.

580, 234 So. 2d 871 (1970); *See Texas National Bank* v. *Fidelity and Deposit Co.*, 526 S.W.2d 770 (Tex. Civ. App. 1975) (bank has burden of proving it sustained loss *through* its acceptance of forged securities); *Cf. Lyndonville Savings Bank and Trust Co.* v. *Peerless Insurance Co.*, 126 Vt. 436, 234 A.2d 340 (1967) (bank must prove elements of the crime of false pretenses to recover on bankers blanket bond for loss resulting from payment for a bad check). Conversely, where the bankers bond policy has an express exclusion for losses caused by forgery, the burden to prove the forgery, and therefore the exclusion of coverage, is on the insurer. *United Pacific Insurance Co.* v. *Idaho First National Bank*, 378 F.2d 68 (9th Cir. 1967) (applying Idaho law).

Although we find no Tennessee cases which squarely address the question of whether the plaintiff bears the burden of proving that there was a forgery in order to recover under a bankers blanket bond we do find that Tennessee law is in accord with the general rule regarding the allocation of the burden of proof in insurance claims. Tennessee case law recognizes that the burden is on the insured to prove the essential elements of his cause of action to recover on an insurance policy. *Curtis* v. *American Casualty Co.*, 60 Tenn. App. 204, 445 S.W.2d 661 (1968) (life insurance claim). *See Hurt* v. *Merchants and Manufacturers Insurance Co.*, 188 Tenn. 572, 221 S.W.2d 808 (1949) (automobile insurance claim). Specifically, the claimant must prove the existence and validity of the insurance policy, *Epstein* v. *Great American Insurance Co.*, 54 Tenn. App. 447, 392 S.W.2d 331 (1965), the extent or amount of loss where the fact is in issue, *Shirley* v. *American Central Insurance Co.*, 21 Tenn. App. 259, 109 S.W.2d 100 (1937) and that the death or injury of the insured was the result of a cause, and was sustained in a manner, covered by the policy. *Gilmore* v. *Continental Casualty Co.*, 188 Tenn. 588, 221 S.W.2d 814 (1949); *McFarland* v. *Massachusetts Bonding & Insurance Co.*, 157 Tenn. 254, 8 S.W.2d 369, 64

ALR 962 (1928); *Reserve Life Insurance Co.* v. *Whittemore*, 59 Tenn. App. 495, 442 S.W.2d 266 (1969); *Woodward* v. *Interstate Life and Accident Co.*, 25 Tenn. App. 120, 152 S.W.2d 636 (1941); *Bell* v. *Travelers' Insurance Co.*, 18 Tenn. App. 552, 79 S.W.2d 824 (1935). Tennessee also recognizes the general rule that the burden of establishing that a loss resulted from a cause falling within a policy exclusion is on the insurer, *Freeze* v. *Continental Casualty Co.*, 5 Tenn. App. 261 (1927), and therefore to avoid liability the insurer has the burden of proving that the insured's death or injury resulted from a risk excluded from an accident insurance policy. *Interstate Life and Accident Insurance Co.* v. *Gammons*, 56 Tenn. App. 441, 408 S.W.2d 397 (1966) (exclusion for injuries resulting from intoxication). Therefore, we think it is clear that Tennessee law on the subject of allocation of burden of proof in insurance cases is in accord with generally accepted rules.

It appears, moreover, that when the issue of forgery arises in a suit to collect a note, Tennessee law places "the burden of proof on the complainant with respect to the execution of the note." *Phillips* v. *Tidwell*, 26 Tenn. App. 543, 174 S.W.2d 472, 477 (1942). Thus general insurance law and principles of Tennessee contract law would place the burden of proof on the plaintiff bank to show that the bill of sale was forged. The District Court improperly placed the burden of proving a forgery on the defendant, Transamerica.

It remains to consider whether the bank proved a forgery. There is no need to remand this case for the purpose of giving the bank the opportunity to meet its burden of proof. All the significant testimony was submitted by deposition and the District Court did not conclude that the defendant bore the burden of proof during the course of trial, but in its memorandum opinion. There is no indication that the bank would have presented any additional evidence or that it expected the burden of proof to be placed on the defendant.

Neither Hill, who was murdered shortly before trial, nor Herring, who was serving a sentence in a federal penitentiary for fraud and who had invoked his Fifth Amendment privilege, testified as to this or any other issue. The bank solicited testimony from two indivduals concerning whether Herring was authorized to sign Hill's name to the contract of sale. Mrs. Hill, David Hill's wife, testified that she did not know, and had no reason to know, whether her husband ever authorized someone else to sign his name. Similarly, Mr. Daniel Hatcher, a notary public who had notarized the false bills of sale, testified that the signature on the bill of sale was not that of David Hill, that he did not specifically recall notarizing the document, but that he would not have notarized it if Mr. Hill had not specifically given authority for someone else to sign his name. It is fair to conclude that this evidence, properly viewed, does not establish a lack of authority. Mrs. Hill's testimony is not probative because, as she admitted, she knew nothing of her husband's business practices. Mr. Hatcher's testimony establishes the *existence* of authority as opposed to negating its existence. In short, the bank's evidence did not establish lack of authority as an element of forgery.

Transamerica's proof on rebuttal is strong. Transamerica presented evidence that Herring and Hill worked out an almost identical scheme to defraud the CIT corporation. In the previous scheme Herring signed Hill's name as purchaser – this time to five conditional sales contracts. The contracts were for non-existent equipment. The conditional sales contracts were then sold to CIT by Herring, making CIT Hill's creditor with non-existent bulldozers for security. Although Hill had not actually signed the conditional sales contracts he nonetheless made payments to CIT, using money funneled to him by Herring. Hill ultimately defaulted in his payments to CIT. These facts present a pattern strikingly similar to the present case. The defendant presents strong evidence

that in the scheme against CIT Hill authorized Herring to sign his name, and this evidence raises a strong inference that similar authorization was given here.

There is also the direct evidence of the notary public, Hatcher, that he would not have notarized the signature of Hill's name on the bill of sale unless Hill had authorized him to do so. Then there is the strong circumstantial evidence arising out of the phony paper transaction. The scheme began with Hill "selling" the equipment to Herring, d/b/a Herco, who then engaged in a sale/leaseback transaction with SLC. Finally, and most damaging, Herring subleased the non-existent equipment back to Hill. The only logical reason Hill would accept a sublease of non-existent equipment, which carried with it sixty lease payments of at least $8,000 each, is that he was a full partner in the fraud and either had authorized Herring to sign his name, or ratified the signature.

Therefore, we conclude that the plaintiff did not carry its burden of proof that Hill's signature on the bill of sale constituted a forgery.

Accordingly, the judgment of the District Court is reversed.

No. 80-5486

UNITED STATES COURT OF APPEALS

FOR THE SIXTH CIRCUIT

FARMERS BANK & TRUST COMPANY OF WINCHESTER, TENNESSEE,	)	
Plaintiff-Appellee	)	ORDER DENYING PETITION FOR REHEARING
v.	)	
TRANSAMERICA INSURANCE COMPANY,	)	
Defendant-Appellant	)	

Before: MERRITT and JONES, Circuit Judges; TAYLOR, District Judge*

Upon consideration of the petition for rehearing filed herein by the plaintiff-appellee, the Court concludes that all of the questions addressed in the petition for rehearing were fully considered upon the original submission and decision of this case.

*The Honorable Anna Diggs Taylor, Judge, United States District Court for the Eastern District of Michigan, sitting by designation.

It is therefore ORDERED that the petition for rehearing be and it hereby is denied.

ENTERED BY ORDER
OF THE COURT

/s/ John P. Hehman
Clerk

AFFIDAVIT OF SERVICE

I, Robert S. Peters, attorney for the petitioner herein, depose and say that on the 17th day of August, 1982 I deposited three (3) copies of the Petition for Certiorari to counsel of record for the respondent at his post office address.

Robert S. Peters

Subscribed and sworn to before me, this 17th day of August, 1982.

Frances McCain
Notary Public

My Commission Expires: April 24, 1984.